

**GOVERNMENT OF THE DISTRICT OF COLUMBIA  
OFFICE OF THE INSPECTOR GENERAL**

**District of Columbia Public Schools**

**Material Weaknesses and  
Reportable Conditions in Internal Control  
Over Financial Reporting and  
Management Letter Comments**

**for the year ended September 30, 2005**



**CHARLES J. WILLOUGHBY  
INSPECTOR GENERAL**

**GOVERNMENT OF THE DISTRICT OF COLUMBIA**  
**Office of the Inspector General**

Inspector General



April 10, 2006

Clifford B. Janey, Ed.D.  
Superintendent  
District of Columbia Public Schools  
825 North Capitol Street, N.E., 9th Floor  
Washington, D.C. 20002

Natwar M. Gandhi, PhD.  
Chief Financial Officer  
Office of the Chief Financial Officer  
1350 Pennsylvania Avenue, N.W., Room 203  
Washington, D.C. 20004

Dear Dr. Janey and Dr. Gandhi:

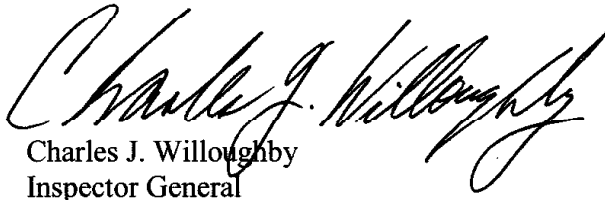
In conjunction with the audit of the District of Columbia Public School's (DCPS) Budgetary Comparison Schedule – Governmental Funds and Supplemental Information (With Independent Auditor's Report Thereon) for the fiscal year ended September 30, 2005, BDO Seidman, LLP submitted the enclosed Reports: *Material Weaknesses and Reportable Conditions in Internal Control Over Financial Reporting and Management Letter Comments*. These reports provide information about DCPS's compliance with laws and regulations and the adequacy of internal controls, and also recommend actions to improve DCPS operations.

BDO Seidman set forth recommendations for correcting reportable conditions and other deficiencies. In most cases, DCPS responded favorably to the recommendations contained in the reports and, in some cases, corrective action has already been taken to remedy the issue. However, management did not concur with recommendations relative to supervisory review of journal entries, application of indirect cost rates, and the receivables and revenue cut-off process. Additionally, management has not responded favorably to prior-year recommendations pertaining to tracking of personnel movement and Statements in Accounting Standards (SAS) 70.

Accordingly, we request that DCPS and the Office of the Chief Financial Officer provide an updated response to these recommendations, as well as estimated target completion dates to correct the conditions noted. We ask that this information be provided to this Office within 60 days from the date of this letter. While the Office of the Inspector General will continue to assess DCPS's implementation of recommendations, it is DCPS's responsibility to ensure that the deficiencies noted in audit reports are corrected.

If you have any questions, or need additional information, please contact me, or have a member of your staff contact William J. DiVello, Assistant Inspector General for Audits, at (202) 727-2540.

Sincerely,



Charles J. Willoughby  
Inspector General

CJW/ws

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April 10, 2006  
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Accountants and Consultants

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January 19, 2006

To the Members  
**Board of Education of the District of Columbia**  
825 North Capitol Street, NE  
Washington, D.C. 20002

In planning and performing our audit of the Budgetary Comparison Schedule – Governmental Funds (the Schedule) of the **District of Columbia Public Schools (DCPS)**, an agency of the Government of the District of Columbia for the year ended September 30, 2005, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the Schedule and not to provide assurance on internal control. However, we noted certain matters involving internal control and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control that, in our judgment, could adversely affect DCPS' ability to initiate, record, process, and report financial data consistent with the assertions of management in the Schedule.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of internal control would not necessarily disclose all matters that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses, as defined above. In addition, because of inherent limitations in internal control, errors and fraud may occur and not be detected by such controls. However, we noted the following reportable conditions, described in greater detail in Appendix A, which we believe to be material weaknesses.

- I. Retroactive Payment of Salary Step Increases
- II. Benefit Payments for Inactive Employees

We also noted the following reportable condition, described in greater detail in Appendix A, which is not believed to be a material weakness.

- III. Official Personnel Folders and Inadequate Supporting Documentation

These material weaknesses and the other reportable condition were considered in determining the nature, timing, and extent of tests applied in our audit of the Schedule, and this report does not affect our report on the Schedule, which is also dated January 19, 2006. We have not considered internal control since the date of our report.

We have also prepared suggestions for improvements in DCPS' internal control that we did not consider to be reportable conditions or material weaknesses. These are presented in Appendix B for your consideration. The status of prior year material weaknesses, reportable conditions, and advisory comments is presented in Appendix C.



**BDO Seidman, LLP**  
Accountants and Consultants

This letter is intended solely for the information and use of the Board of Education of DCPS, the management of DCPS, the Mayor and Council of the District, and the Office of Inspector General of the District, and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

*BDO Seidman, LLP*

**BDO SEIDMAN, LLP**



## **Material Weaknesses and Reportable Conditions in Internal Control Over Financial Reporting**

### **I. Retroactive Payment of Salary Step Increases**

#### Observation:

DCPS' payroll system, Comprehensive Automated Personnel and Payroll System (CAPPS) does not appear capable of detecting and calculating employee step increases in a timely manner. Accordingly, the process is performed manually by a limited Human Resources (HR) staff for over 10,000 employees. This results in severe limitations in tracking and budgeting of staff, adequate employee payroll history, proper payroll processing, and calculation of retroactive pay.

At September 30, 2005, accrued retroactive step increases were approximately \$2.0 million, which marked a decrease from the prior year due to a concerted effort by DCPS to process amounts accrued and unpaid from years past. As a result, payroll expenditures reported in SOAR throughout the year and used by management for financial and budgetary analysis are not complete. Because there is a significant understatement of payroll costs incurred throughout the year, this can affect the operational decisions made based on actual to budgetary amounts.

#### Recommendation:

We recommend that an automated document preparation and personnel management system be considered for DCPS. Adopting such a system will ensure that employee step increases are processed in a timely manner. This would also reduce the likelihood of overpayments of retroactive pay due to the tedious and manual (paper) process currently being utilized.

#### Management's Response:

Management concurs with the finding. The Office of Human Resources is hopeful that funding can be secured in the fiscal year 2007 budget so that we may transition from CAPPS to PeopleSoft.

### **II. Benefit Payments for Inactive Employees**

#### Observation:

Per external reports prepared outside of DCPS, it has been determined that approximately \$2.6 million in unnecessary benefits payments were made during fiscal year 2005. These payments relate to benefits being paid to employees no longer with DCPS. CAPPS does not have the capability of processing and sending notifications to the respective personnel and payroll divisions that benefits should be terminated in a timely manner.

Accordingly, a manual process is being utilized where when an employee is terminated or resigns, the staffing division of HR may receive notice and change the employees' status in the personnel system. However, it was noted that this notice is not distributed to other Human Resource (HR) Divisions and is not received for every instance.

#### Recommendation:

We recommend that DCPS adopt a policy to provide all the respective divisions with the necessary documentation to properly terminate benefits for ineligible employees. Ineligible employees who continue to receive benefits place an unnecessary burden on DCPS finances.





## **Material Weaknesses and Reportable Conditions in Internal Control Over Financial Reporting**

### **II. Benefit Payments for Inactive Employees – (continued)**

These resources may be better utilized for an automated personnel and payroll system that captures these errors before the costs become significant.

We note that these have been recurring issues for DCPS which must be addressed to allow management to operate efficiently to accomplish its mission of providing educational services to the District's citizens.

#### Management's Response:

We concur with the findings and agree with the fact that there is a deficiency regarding the capability of the Human Resource Information System to electronically process such data and therefore, we must resort to creating a paper driven information system which is not as timely as industry standards require to notify all affected offices of the respective personnel changes.

HR has developed and is currently refining its notification process. Within 31 days of receiving notification that an employee has separated from service, HR will manually generate the personnel action report terminating their employment. The personnel action report will be sent to all appropriate divisions, including Benefits, Payroll, and the Office of Pay and Retirement within 7 business days of its generation. In addition, HR will terminate an employee's record within 30 days of generating the personnel action report, thus eliminating the overpayment in benefits.

Until October of last year, our division had not been receiving the Health Benefits Paid Report on a regular basis. We now perform periodic reconciliations and as a result of these reconciliations we have been credited with \$1.4 mil (plus) in over paid premiums. As of October 2005, the premiums were hovering at \$80,000 (plus) per pay period. This number increases in July and August because of 10-month employees. Our division requested and is now receiving the Health Benefits Paid report. Because we are now reviewing the report and comparing each name to the payroll record, we have been able to reduce the number to just less than \$30,000.

Additionally, we are more conscious of the fact that more effective communication must occur between the various elements of staffing and benefits administration to preclude further deficiency.

### **III. Official Personnel Folders and Inadequate Supporting Documentation**

#### Observation:

- We selected a sample of 125 files of newly hired employees to determine whether supporting documentation authorizing payroll action (Form 52 – Request for Employment Action or equivalent) had been completed. We determined that 31 files did not contain the Form 52 or equivalent document, authorizing payroll action for the hired employees.
- In addition, we selected a sample of 97 files of terminated employees to determine whether supporting documentation authorizing the change in status from active to inactive employee had been completed. We determined that 83 files did not contain the Form 1 (Personnel Action) or equivalent document, authorizing the change in status from active to inactive employee.



**Material Weaknesses and Reportable Conditions  
in Internal Control Over Financial Reporting**

**III. Official Personnel Folders and Inadequate Supporting Documentation – (continued)**

- We also noted that 51 of the 125 files did not contain a completed Employment Eligibility Verification Form I-9 documenting that the employee was eligible for employment with DCPS.

Maintaining adequate supporting documents authorizing the processing of payroll for new and terminated employees is essential to ensure accurate payment of the bi-weekly payroll. Without this documentation on file, errors in payroll may not be detected in a timely manner and may result in improper payments to current and terminated employees.

We also noted that the Human Resources department has operated without a formal policy and procedures manual.

Recommendation:

We recommend that DCPS consider a system similar to the District of Columbia Office of Financial Operations and Systems (OFOS) that allows for truly automated document preparation and personnel management functions. In addition, the system will allow for greater flexibility in tracking active teachers within the school system.

We also recommend that management establish a standard operating procedures manual outlining policies to be followed. Written procedures, instructions, and assignments of duties will prevent or reduce misunderstandings, errors, inefficient or wasted effort, duplicated or omitted procedures, and other situations that can result in inaccurate or untimely accounting records. A well-devised manual can help to ensure that all similar transactions are treated consistently and that records are produced in the form desired by management. A good manual should also aid in the training of new employees.

Management's Response:

Management concurs with the finding. The Office of Human Resources agrees with the finding and is planning to develop a policy and procedures manual. In addition, the Office of Human Resources is hopeful that funding can be secured in the fiscal year 2007 budget to accomplish the project.



## Advisory Comments

### I. Supervisory Review of Journal Entries

Observation:

We selected a sample of 45 journal entries and tested controls over the review, approval, and posting process. We noted that 1 of the approved journal entries did not agree to the accounting system.

After the journal entry was reviewed by a supervisor, the accountant entered in the same journal entry twice. The error was realized by the accountant during our test work and the duplicate entry was properly reversed. As a result, the journal entry numbering system was thrown off and the entry that was approved contained the incorrect journal entry number. The journal entry form was not corrected with the new journal entry number nor was there any evidence to reference to the corrected journal entry.

We identified this discrepancy from a sample of transactions that were selected for testing. Management should recognize that the potential exists for additional discrepancies.

Recommendation:

DCPS should consider implementing a policy that would allow a supervisor to review and approve all entries in the accounting system after they have been entered, but before they become permanent.

Management's Response:

The Office of Chief Financial Officer (OCFO) disagrees and takes exception to the audit finding. The finding highlights a one time instance, and during this finding, we had not finalized our fiscal year 2005 closing. The OCFO has a system in place to ensure incompatible duties are performed among different individuals. All journal entries are reviewed and approved by the Accounting Officer before posting. Under normal circumstance, the Auditor typically waits to audit the ending balances until we finish our closing process. The transaction in question was identified and corrected during fiscal year 2005. It is also important to notice that DCPS/OCFO reconciled all accounting records at the end of the closing.

### II. Application of Indirect Cost Rates

Observation:

We obtained the 2005 DAFR 520 report for authorized federal expenditures to determine whether the proper indirect cost rate was applied to federal grants for the fiscal year. We noted that the base amount used to calculate the indirect cost rate excluded allowable expenditures which understated the reimbursable rate DCPS was entitled to receive. We also then obtained the 2004 DAFR 520 report and noted this reimbursable rate was also understated. It appears that this situation is due to a prematurely calculated base amount being used prior to the final fiscal year closing.

Recommendation:

We recommend that management adopt a policy to calculate its indirect cost rate once all allowable expenditures have been recorded and charged to federal grants as of the fiscal year closing date. This will allow DCPS to properly charge the maximum allowable indirect cost rate.



## Advisory Comments

### II. Application of Indirect Cost Rates – (continued)

#### Management's Response:

The Office of Chief Financial Officer (OCFO) disagrees and takes exception to the audit finding and recommendation. The finding highlights an instance before we finalized our year-end closing. It is the OCFO's intention to update the indirect cost allocation periodically. Since we did not complete our year-end closing, we did not finalize the allocation of indirect costs. On several occasions, we communicated to the Audit Team our intention and the ongoing closing process. The OCFO has a system in place to ensure that indirect costs are allocated accurately. It is impractical to know the proper base before completion of the year-end closing. The DCPS/OCFO management has been proactive in reviewing all aspects of accounting and finance. We believe it is good financial management to allocate indirect costs periodically.

### III. Receivables and Revenue Cut-off Process

#### Observation:

We noted a rebate amount from Verizon for approximately \$0.9 million that was received on October 12, 2005, and related to the prior fiscal year. This amount was not recognized as a receivable as of the end of the fiscal year resulting in an audit adjustment. In addition, approximately \$0.3 million of Medicaid receivables that were due from another District agency were not properly recorded as of year-end.

#### Recommendation:

We recommend that management thoroughly review receipts that come in after year-end in order to ensure the proper recording of these amounts. In addition, the period of service for Medicaid amounts billed should be reviewed in order to ensure the proper recording of receivables as of year-end.

#### Management Response:

The Office of Chief Financial Officer (OCFO) disagrees and takes exception to the audit finding and recommendation. The finding highlights a one time instance before we finalized our closing. The transaction in question is corrected and booked in fiscal year 2005.

### IV. Medicaid Cost Reports

#### Observation:

Medicaid regulations require submission of cost reports to be done within 5 months of the cost reporting fiscal year end or 30 days after a valid Provider Statistical and Reimbursement Report (PS&R) is sent to the provider by the intermediary (whichever is later). As of December 2005, DCPS had not filed the fiscal year 2003 & 2004 cost reports. We further noted that during fiscal year 2005, the fiscal year 2002 cost report was submitted.

DCPS is in direct violation of compliance with its filing requirements. In addition, the longer that DCPS waits to submit these cost reports, the greater the risk increases that DCPS may not be able to locate the appropriate documentation during the respective cost report audit.



**Advisory Comments**

**IV. Medicaid Cost Reports – (continued)**

**Recommendation:**

We recommend that DCPS gather the information needed to file a complete and accurate cost report and file these reports that are past due. Going forward, an effort should be made to file these reports within the regulated time frame. The Medicaid Recovery Unit (MRU) has represented that it is in the process of compiling these reports for submission.

**Management Response:**

DCPS agrees with the audit finding and recommendation. The Medicaid Recovery Unit (MRU) is in the process of finalizing the 2003 cost report. MRU is filling all staff vacancies following the appointment of a new acting director. Once all positions are filled, work on the 2004 cost report shall commence. It is anticipated that the 2003 report will be submitted by March 31, 2006 and the 2004 report submitted before the end of this year. DCPS has a two year window to submit claims and wants to ensure that all claims for a particular fiscal year are adjudicated prior to submitting a cost settlement report for that year.



**Status of Prior Year Comments**

<u>Nature of Comment</u>	<u>Type of Comment in Fiscal Year 2004</u>	<u>Current Year Status</u>
Inadequate Monitoring of Budgeted and Actual Expenditures	Material Weakness	Resolved
Retroactive Payment of Salary Step Increases	Material Weakness	Material Weakness
Improper Use of Direct Disbursements	Reportable Condition	Resolved
Inadequate Inventory Control	Reportable Condition	Resolved
Insufficient Tracking of Personnel Movement	Reportable Condition	Reportable Condition *
Improper Use of Advanced Funds	Reportable Condition	Resolved
Lack of Controls over Sole Source Contracts and Contract Modifications	Reportable Condition	Resolved
Lack of Approval and Segregation of Duties over Manual Journal Entries	Reportable Condition	Advisory Comment
Checks Outstanding for Greater than 60 Days Remain Uncleared	Advisory Comment	Resolved
Official Personnel Folders and Inadequate Supporting Documentation	Reportable Condition	Reportable Condition
Lack of Provider SAS 70 Report	Advisory Comment	Advisory Comment *
Accrued Liabilities Overstated	Advisory Comment	Resolved

\* - These represent findings from the prior year noted again in fiscal year 2005. Management represented in the prior year that it is comfortable with current procedures. Management continues with this position in fiscal year 2005 and no changes will be implemented.